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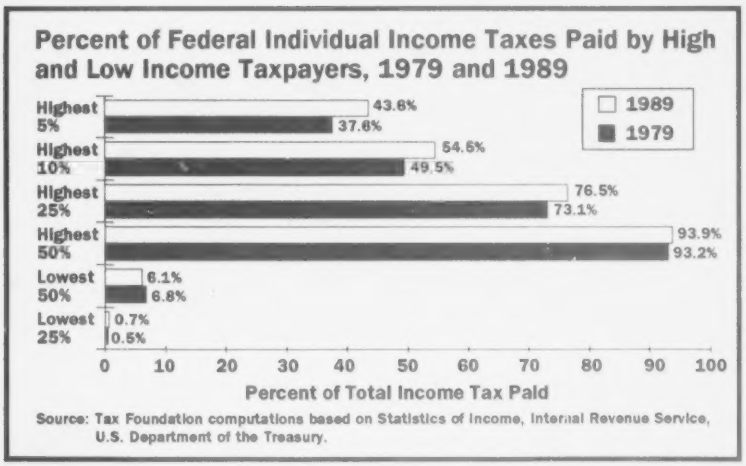
# Tax Features

## Top Tenth of Taxpayers Pays Over Half of Individual Income Taxes

### *Top Half Pays Over 90 Percent*

The top-earning ten percent of U.S. taxpayers paid nearly 55 percent of the federal individual income tax bill in 1989, according to Tax Foundation analysis of the recently released 1989 IRS tax return data. Despite all the major tax legislation witnessed over the decade of the 1980s, the fraction of income taxes collected from this top ten percent varied only slightly from year to year between 1979 and 1989 but inched steadily up during the decade.




Source: Tax Foundation computations based on Statistics of Income, Internal Revenue Service, U.S. Department of the Treasury.

After paying 49.5 percent of all federal individual income taxes collected in 1979, these taxpayers, who now number 11.2 million, put a little more into the till most years until in 1989 they paid 54.5 percent. While their adjusted gross income (AGI) rose 89 percent from 1979 to 1989, their average tax payment rose even more — 94 percent — and averaged $22,225 in 1989. Their AGI ranged down to $61,780, not exactly "fat cat" status. It still takes millions of middle and upper-middle income taxpayers to pay the bulk of the total income tax bill.

All segments of the top earning half paid a

*See Tax Burdens on page 5*

**Tax Foundation**

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FRONT BURNER

## Encourage Savings Without Penalties

*Senator Bob Packwood*

Since I've been in Congress, we have tried many tax incentives to encourage Americans to save more. One of the more successful ideas is the tax-deferred savings plan, exemplified by 401(k) and 403(b) savings plans and Individual Retirement Accounts (IRAs). There is almost $600 billion now in those savings plans.

But many Americans, and especially younger workers, are reluctant to use these savings plans. For example, less than seven percent of younger workers (under age 35) contribute to an IRA. Why? Because they do not want to be hit with a 10-percent "early withdrawal penalty" if they withdraw their money before retirement, generally, age 59 1/2.

Most younger Americans have a difficult time making ends meet. They are just starting out in their careers. They are in their early years of parenting. Their incomes are low and their expenses are high. But, they need to set aside funds for unforeseen events, such as loss of employment or high medical bills. They want to save for a first home. As their children grow up, they must save for their children's college education.

Yet, if Americans put money in a tax-deferred savings plan, the tax code punishes them for withdrawing money for these purposes by imposing a 10-percent penalty.

This is not right. We should encourage Americans to save, not penalize them. It's become more and more difficult for them to save. For example, home ownership among

*See Packwood on page 2*

***Senator Bob Packwood, Republican from Oregon, is the Ranking Minority Member of the Senate Finance Committee.***

*The opinions expressed in the Front Burner are not necessarily those of the Tax Foundation. Editorial replies are encouraged.*

*Packwood from page 1*

younger families has declined 15 percent over the last eight years. We cannot afford to let this trend continue.

In my home state, the timber industry has fallen on hard times. The number of unemployed timber workers will only continue to grow. Those who were fortunate enough to put aside funds in an IRA or similar account need every penny of those funds to put food on their family's table. It's ridiculous to make them pay 10-percent of their savings to the federal government.

***"Less than seven percent of younger workers (under age 35) contribute to an IRA. Why? Because they do not want to be hit with a 10-percent "early withdrawal penalty" if they withdraw their money before retirement."***

Health care expenses in this country have continued their double-digit increase. Employers are attempting to deal with these rising costs by increasing the employee's deductibles and co-insurance. For many employees, payment of these out-of-pocket costs for a prolonged illness or numerous medical problems can be financially devastating. Families should be able to use their savings to meet these needs without penalty.

***"Home ownership among younger families has declined 15 percent over the last eight years. We cannot afford to let this trend continue."***

Education expenses at colleges and universities are another significant out-of-pocket cost for families. The annual cost of a college education is now between $6,000 and $15,000. A recent survey found that only half of the parents who hope to send their children to college have saved even a small portion of the amount needed for tuition, room and board, and books. We must do more to encourage families to save.

IRAs are just one vehicle for savings. Others, such as 401(k) plans, have been growing in popularity during the 1980s and have proven to be an effective way to save. 401(k) plans are now offered by over 50 percent of employers with more than 250 employees, and by more than 90 percent of large employers. The problem with IRAs and tax-deferred savings plans such as 401(k) and 403(b) savings plans is that the incentive to save is limited to retirement. The savings put into these plans cannot be withdrawn for other purposes without the saver suffering a serious financial penalty.

***"Younger Americans . . . want to save for a first home. As their children grow up, they must save for their children's college education. . . Yet, if Americans put money in a tax-deferred savings plan, the tax code punishes them for withdrawing money for these purposes by imposing a 10 percent penalty. That is not right."***

***"A recent survey found that only half of the parents who hope to send their children to college have saved even a small portion of the amount needed for tuition, room and board, and books. We must do more to encourage families to save."***

The legislation I propose will allow Americans to use 401(k) and 403(b) savings plans and IRAs to save for the following purposes without incurring a 10-percent penalty:

1. Purchase of a first home by the taxpayer and the taxpayer's spouse, child or grandchild.

***"In my home state, the . . . number of unemployed timber workers will only continue to grow. Those who were fortunate enough to put aside funds in an IRA or similar account need every penny of those funds to put food on their family's table. It's ridiculous to make them pay 10-percent of their savings to the federal government."***

2. Periods of unemployment of the taxpayer lasting longer than six months.
3. Catastrophic medical expenses.
4. College education for the taxpayer and the taxpayer's spouse, child or grandchild.

Amounts withdrawn penalty-free because of unemployment could be repaid to the account within one year of returning to employment. Repaid amounts would be tax deductible.

The idea of allowing penalty-free withdrawals from retirement savings accounts for special needs is not a new one. My bill incorporates the best features of various proposals, and I strongly believe that enacting this legislation will encourage Americans to save more and strengthen the U.S. economy.

**Mark Your Calendars**
**November 20, 1991**
**for the**
**Tax Foundation's**
**54th Annual Dinner &**
**43rd National Conference**
**at the Waldorf-Astoria**
**in**
**New York City**

# Foundation Promotes Sound Research and Development Tax Policy Before Ways and Means Committee

Dr. B. Anthony Billings, senior research fellow at the Tax Foundation and professor of tax accounting at Wayne State University, appeared before the Ways and Means Committee on July 17 to testify on U.S. international competitiveness. He emphasized the vital role that U.S. R&D tax policy could play in boosting U.S. competitiveness and compared U.S. R&D spending with that of selected major trading nations (see figure below).

Billings pointed out that the U.S. has been losing market share of technologically intensive products, an area which he asserts is particularly sensitive to our nation's R&D tax policy, which has "failed to offer the U.S. private sector adequate economic incentives to encourage R&D activities."

After a study of fourteen industrial groups in Japan and the U.S., Billings concluded that U.S. companies' R&D programs are just as efficient as their Japanese counterparts. He therefore cites U.S. R&D tax policy as responsible for our relatively poor performance in high-tech industries.

He offers three prescriptions:

*Reallocate funds from government-sponsored R&D programs to a tax incentive.* "Most technological breakthroughs result from private-sector projects rather than government-sponsored projects."

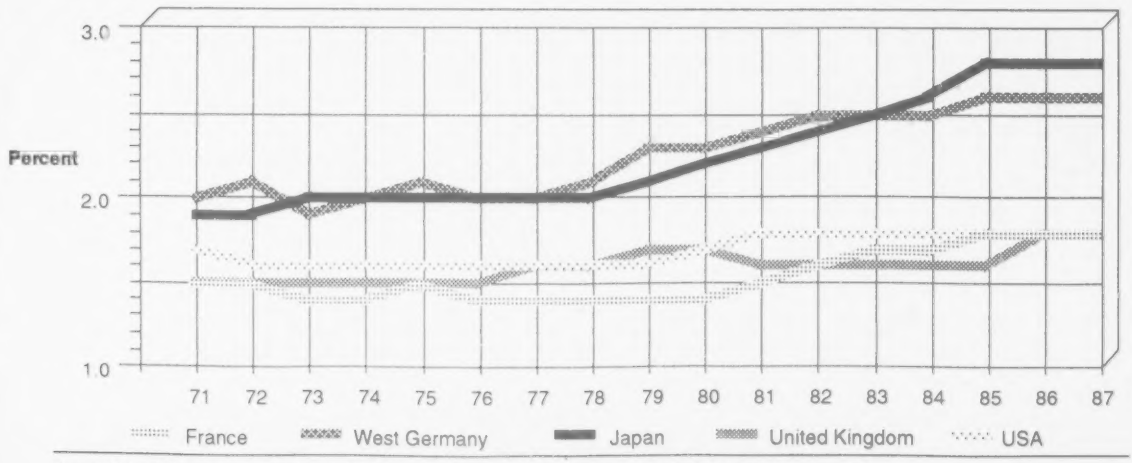
***Dr. B. Anthony Billings, senior research fellow at the Tax Foundation, appears before the House Ways and Committee.***

*Revise the R&D tax credit provisions to allow for a credit based on total R&D.* The current policy of allowing a tax credit only on incremental R&D spending "ignores the nature of R&D spending patterns. A more appropriate approach would be to base the credit on the total R&D outlay in the current period."

*Combine R&D tax incentives with other measures.* One practice of most of our major trading partners is to offer export incentives through the classification of certain sales as foreign source income.

Professor Billings asserted that these changes could be paid for by reallocating funds that are currently devoted to government-sponsored R&D, and that the change "would foster greater efficiency in American industries without a revenue cost to the U.S. Treasury." ■

**Estimated Non-Defense R&D Expenditures as a Percentage of Gross National Product**



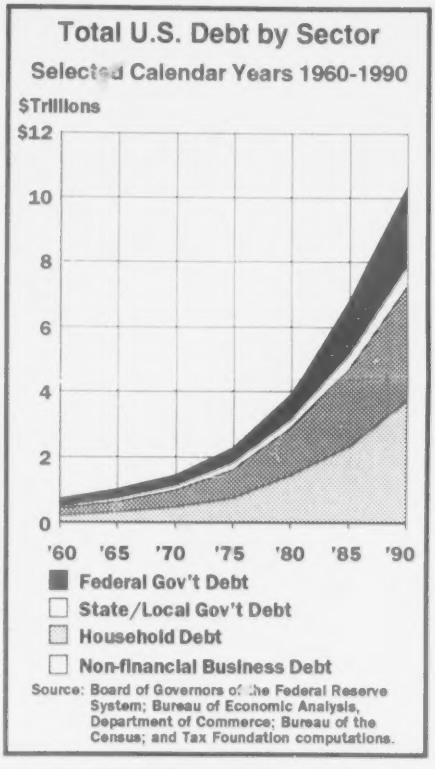

Source: National Science Foundation, International Science and Technology Data Update: 1988, (NSF 89-307), Washington, D.C., 19889.

# Study of U.S. Debt Shows Ten-Year Period of Tremendous Growth

As the nation struggles to work its way out of recession, Americans are feeling the pinch of the $10.6 trillion total U.S. debt, according to a new Tax Foundation report entitled *A Nation in Debt* (6 pp., $10). Fueled by record spending at all levels of government, highly leveraged financing by corporations, and record consumer credit card spending, the debt currently amounts to a $42,277 IOU for every man, woman, and child in the United States.

In the 1980s, total U.S. debt nearly tripled, jumping from $3.9 to $10.6 trillion (see table and figure). Despite the doubling of household and non-financial business debt, their percentage shares of total debt have actually fallen slightly due to the even more rapid increase of the federal government's debt.

The federal government's spending spree during the 1980s tripled its debt from $743 billion in 1980 to $2.5 trillion in 1990, increasing the federal slice of the total debt from 19 to 24 percent. State and local government debt has grown less rapidly, but nevertheless, it has more than doubled during the decade.




### Is U.S. Debt Really Too Large?

As gross national product (GNP) increases, so does an economy's ability to incur debt without seriously impeding economic growth, but the growth in total U.S. debt has steadily outpaced national output. The debt is currently almost double the nation's $5.4 trillion GNP.

In 1990, the federal government made net interest payments of $186.3 billion, or 15 cents of every dollar it spent. By comparison, it only spent 9 cents per dollar on interest in 1980. Unlike the federal government, state and local governments earned more interest than they paid out, generating $41.6 billion in 1990 revenues.

### The Federal Debt

Between 1980 and 1990, the federal government's debt almost doubled as a percentage of GNP, increasing from 27 to 45 percent. These figures would not be nearly as surprising if the 1980s had been a period of economic stagnation. On the contrary, GNP grew at the robust rate of 7.4 percent during the decade, but increasingly monumental federal deficits overwhelmed this growth. Starting the

*See U.S. Debt on page 5*

## Total U.S. Credit Market Debt Outstanding by Sector

### Per Capita and Percent of Gross National Product

### Selected Calendar Years 1960-1991

($Billions except per capita)

| | Total Debt Outstanding | | | Federal Government(a) | | | State/Local Governments | | | Households | | | Non-Financial Businesses | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Total | Per Capita | Percent of GNP | Total | Per Capita | Percent of GNP | Total | Per Capita | Percent of GNP | Total | Per Capita | Percent of GNP | Total | Per Capita | Percent of GNP |
| 1960 | $727.3 | $4,026 | 141.1% | $236.3 | $1,308 | 45.9% | $72.0 | $399 | 14.0% | $218.2 | $1,208 | 42.3% | $200.8 | $1,111 | 39.0% |
| 1965 | 1,011.6 | 5,206 | 143.5 | 262.4 | 1,350 | 37.2 | 103.1 | 531 | 14.6 | 343.2 | 1,766 | 48.7 | 302.9 | 1,559 | 43.0 |
| 1970 | 1,424.4 | 6,947 | 140.3 | 300.8 | 1,467 | 29.6 | 150.3 | 733 | 14.8 | 471.8 | 2,301 | 46.5 | 501.5 | 2,446 | 49.4 |
| 1975 | 2,256.0 | 10,446 | 141.1 | 446.3 | 3,068 | 27.9 | 219.4 | 1,016 | 13.7 | 750.4 | 3,475 | 46.9 | 839.9 | 3,889 | 52.5 |
| 1980 | 3,897.7 | 17,116 | 142.7 | 742.8 | 3,262 | 27.2 | 286.6 | 1,259 | 10.5 | 1,430.2 | 6,281 | 52.3 | 1,438.1 | 6,315 | 52.6 |
| 1981 | 4,279.6 | 18,611 | 140.2 | 830.1 | 3,610 | 27.2 | 303.7 | 1,321 | 9.9 | 1,549.2 | 6,737 | 50.8 | 1,596.6 | 6,943 | 52.3 |
| 1982 | 4,667.6 | 20,104 | 147.4 | 991.4 | 4,270 | 31.3 | 331.4 | 1,427 | 10.5 | 1,626.3 | 7,005 | 51.4 | 1,718.5 | 7,402 | 54.3 |
| 1983 | 5,208.5 | 22,230 | 152.9 | 1,177.9 | 5,027 | 34.6 | 355.0 | 1,515 | 10.4 | 1,791.9 | 7,648 | 52.6 | 1,883.7 | 8,040 | 55.3 |
| 1984 | 5,959.4 | 25,215 | 158.0 | 1,376.8 | 5,825 | 36.5 | 383.0 | 1,621 | 10.2 | 2,018.8 | 8,542 | 53.5 | 2,180.8 | 9,227 | 57.8 |
| 1985 | 6,804.5 | 28,534 | 169.5 | 1,600.4 | 6,711 | 39.9 | 473.9 | 1,987 | 11.8 | 2,296.0 | 9,628 | 57.2 | 2,434.2 | 10,208 | 60.6 |
| 1986 | 7,646.3 | 31,772 | 180.7 | 1,815.4 | 7,543 | 42.9 | 510.1 | 2,120 | 12.1 | 2,596.1 | 10,788 | 61.4 | 2,724.8 | 11,322 | 64.4 |
| 1987 | 8,343.9 | 34,362 | 184.8 | 1,960.3 | 8,073 | 43.4 | 558.9 | 2,302 | 12.4 | 2,879.1 | 11,857 | 63.8 | 2,945.6 | 12,131 | 65.2 |
| 1988 | 9,096.0 | 37,119 | 186.6 | 2,117.8 | 8,642 | 43.5 | 604.5 | 2,467 | 12.4 | 3,191.5 | 13,024 | 65.5 | 3,182.2 | 12,988 | 65.3 |
| 1989 | 9,805.3 | 39,641 | 188.5 | 2,269.4 | 9,175 | 43.6 | 634.1 | 2,564 | 12.2 | 3,501.8 | 14,157 | 67.3 | 3,400.0 | 13,746 | 65.4 |
| 1990(b) | 10,317.6 | 41,275 | 188.8 | 2,450.4 | 9,803 | 44.8 | 642.2 | 2,569 | 11.8 | 3,731.8 | 14,929 | 68.3 | 3,493.2 | 13,974 | 63.9 |
| 1991(c) | 10,636.6 | 42,277 | 191.4 | 2,624.7 | 10,432 | 47.2 | 648.6 | 2,578 | 11.7 | 3,860.2 | 15,343 | 69.5 | 3,503.1 | 13,924 | 63.0 |

(a) Federal government debt excludes portion held by Federal Reserve and government agencies.
(b) 1990 figures based on quarterly average.
(c) 1991 figures based on first quarter statistics.
Source: Board of Governors of the Federal Reserve System; Bureau of Economic Analysis, Department of Commerce, Bureau of the Census; and Tax Foundation computations.

*U.S. Debt from p. ge 4*

decade with a $73.8 billion deficit in FY80, lawmakers nearly tripled that deficit in two years. Significant reductions in FY84 and FY87 did not arrest the upward trend, and with an expected FY92 budget deficit of $348 billion, public debt and its associated interest costs are expected to pass the $5 trillion mark by FY95.

While federal debt is the largest portion of U.S. liabilities, it is by no means the total. Accounts payable, pensions, and actuarial liabilities such as veterans compensation bring the total to $3.77 trillion, $1.61 trillion more than the public debt reported, and even this larger figure does not take Social Security into account.

### State and Local Debt

State and local government debt makes up the smallest portion of the debt pie. It totaled $642.2 billion in 1990, and as a percent of GNP, state/local government debt remained at a fairly consistent rate of 11 percent in the past decade. However, in light of the current fiscal crises in many states, debt levels for state governments are likely to grow more rapidly in the 1990s than they did in the 1980s.

### Household Debt

Household debt, comprised mainly of mortgages and consumer credit, increased from 52 percent of GNP in 1980 to 68 percent in 1990. The largest portion of total debt, household debt peaked in 1990 at $3.7 trillion, or $14,929 for every member of the household.

The rise in consumer debt can be illustrated by the rapid jump in credit card usage throughout the 1980s. While credit card spending rose 93 percent, from $205.4 billion in 1980 to $397.1 billion in 1988, credit card debt increased even faster, a 122 percent rise from $81.2 billion to $180 billion. Credit card debt, as opposed to spending, refers to the debit balance amount carried over from month to month.

### Non-Financial Business Debt

Second to households, non-financial business is the largest borrowing sector in the economy. During a decade famous for leveraged buyouts and junk bond financing, debt for non-financial businesses leaped from $1.4 trillion in 1980 to $3.5 trillion in 1990. ■

*Tax Burdens from page 1*

larger share of the income tax bill over the course of the decade. The top five percent paid 43.6 percent in 1989, up from 37.6 in 1979; the top 25 percent paid 76.5 percent of the taxes paid in 1989, compared to 73.1 percent in 1979; and the top half increased its lion's share from 93.2 to 93.9 percent.

The lower half's share of income taxes paid dropped 11 percent over the decade. These taxpayers, whose AGI ranged from $18,851 down to zero in 1989, paid 6.1 percent of total taxes, down from 6.8 percent in 1979. The lowest 25 percent paid a slightly higher percentage of collections, up from .5 percent in 1979 to .7 percent in 1989.

### Trends in Progressivity

The federal income tax system has remained progressive. Top earners continue to pay a larger share of tax collections despite the alleged upper-income bias of the tax cuts and rate reductions under the Economic Recovery Tax Act of 1981 and the Tax Reform Act of 1986.

Growth in the income base itself has been increasing faster at the upper end of the income scale, resulting in increased income tax receipts from top earners. Naturally, this also results in a higher proportion of the entire population's income being taxed at the highest rate.

The 112 million returns filed for tax year 1989 reported an increase in AGI of $194 billion over 1988. The largest percentage gain in income was from Individual Retirement Account distributions, up 24.3 percent from 1988. Social Security benefits rose 22.4 percent, and taxable interest increased 15.5 percent. Salaries and wages, which constituted 71.6 percent of total positive income for 1989, rose 5.5 percent over 1988. All told, 1989 total individual income taxes rose $23.3 billion over 1988 for a record $439 billion take. ■

**Federal Income Taxes Paid by High and Low-Income Taxpayers, 1979 and 1989[a]**

| Adjusted Gross Income Class | Income Level | | Percent of Tax Paid | | Average Tax | |
|---|---|---|---|---|---|---|
| | 1979 | 1989 | 1979 | 1989 | 1979 | 1989 |
| Highest 5% | $39,000 or more | $77,568 or more | 37.6% | 43.6% | $17,407 | $35,541 |
| Highest 10% | 32,710 or more | 61,780 or more | 49.5 | 54.5 | 11,456 | 22,225 |
| Highest 25% | 21,760 or more | 37,064 or more | 73.1 | 76.5 | 6,769 | 12,470 |
| Highest 50% | 11,870 or more | 18,852 or more | 93.2 | 93.9 | 4,315 | 7,658 |
| Lowest 50% | 11,869 or less | 18,851 or less | 6.8 | 6.1 | 313 | 496 |
| Lowest 25% | 5,565 or less | 8,465 or less | 0.5 | 0.7 | 46 | 122 |
| Lowest 10%[b] | 2,212 or less | 3,047 or less | c | c | 9 | 43 |

[a] Data for 1989 are preliminary.
[b] Includes returns showing no adjusted gross income.
[c] Less than .1 percent.
Source: Tax Foundation computations based on Statistics of Income, Internal Revenue Service, U.S. Department of the Treasury.

**1989 Income Tax Data**

| Adjusted Gross Income Class | Total Individual Returns (thousands) | Total Adjusted Gross Income ($billions) | Percent of Adjusted Gross Income | Average Tax Rate |
|---|---|---|---|---|
| Highest 5% | 5,614 | $933.7 | 28.4% | 21.4% |
| Highest 10% | 11,228 | 1,278.3 | 38.9 | 19.5 |
| Highest 25% | 28,070 | 2,067.5 | 62.8 | 16.9 |
| Highest 50% | 56,140 | 2,833.1 | 86.1 | 15.2 |
| Lowest 50% | 56,140 | 458.3 | 13.9 | 6.1 |
| Lowest 25% | 28,070 | 82.5 | 2.5 | 4.1 |
| Lowest 10%[a] | 11,228 | -13.8 | - | - |

[a] Includes returns showing no adjusted gross income.
Source: Tax Foundation computations based on Statistics of Income, Internal Revenue Service, U.S. Department of the Treasury.

# Tax Foundation Pursues State Tax Policy Issues in Illinois

Just days after Illinois lawmakers had wrapped up a hard-fought budget battle in Springfield, they repaired to Chicago to join corporate executives, university scholars, and members of the business press at a Tax Foundation program on state tax policy on the afternoon of July 24th. The overall theme was the relationship of tax policy to economic growth, and more specifically, how Illinois had mired itself in fiscal problems and to what extent the new budget would extricate it.

***"[With the new tax impact statements] citizens can now go to those local government budget meetings in advance of final adoption, and do the howling that they have only been able to do when they receive their tax bills."***

***— Jim Nowlan, President, Taxpayers' Federation of Illinois***

### The State Budget in Crisis

"Illinois' Ailing Fiscal Condition — Is There a Cure?" was the question posed to the first panel. The subject was addressed by Dawn Clark Netsch, Comptroller, State of Illinois; Richard S. Winder, Director of State and Local Taxes, Household International; Sen. Howard W. Carroll, Chairman, Appropriations Committee, Illinois General Assembly; James D. Nowlan, President, Taxpayers Federation of Illinois; Patrick Quinn, Treasurer, State of Illinois; and John Skorburg, Chief Economist, Chicago Association of Commerce and Industry.

*From left: Thomas A. Dowd, Vice President - Corporate Tax, CNA Insurance; Dawn Clark Netsch, Comptroller, State of Illinois; Mark Hornung, Associate Editor, Crain's Chicago Business; Dan Witt, Executive Director, Tax Foundation; and Sen. Howard W. Carroll, Chairman, Appropriations Committee, Illinois General Assembly.*

***"Nine of the last eleven fiscal years . . . we have spent more than we have received."***

***— Dawn Clark Netsch, Illinois State Comptroller***

Mark Hornung, Associate Editor of *Crain's Chicago Business* moderated the panel and gave a brief rundown of the new state budget's highlights in his introduction. "About $13 billion of a total $27 billion budget will be spent for general revenue purposes. Of that $13 billion, approximately $6 billion will be spent on human services, $5 billion on education, and more than $2.4 billion on administrative costs of government. . . . There was a budget deficit of $1.8 billion . . . . Approximately $600 million in health care costs are being moved off the general revenue ledger to a new assessment system. . . . $400 million will be closed by creative accounting. . . . Finally, the last $800 million are assorted amounts of cuts. The lion's share of the cuts, about $380 to $400 million, came in the area of human services . . . [with] the remaining $400 to $420 million in cuts coming from assorted areas of government."

*From left: Paul Merski, Director of Fiscal Affairs, Tax Foundation; Dawn Clark Netsch, Comptroller, State of Illinois; Mark Hornung, Associate Editor, Crain's Chicago Business; and John Skorburg, Chief Economist, Chicago Association of Commerce and Industry.*

### From Short-Term Repair to Long-Term Strategies

"Mapping Out Long-Term Policies for Economic Growth" was the theme of the second panel. James L. Johnston, Senior Economist, Amoco Corporation, moderated the panel which included Toni Hartrich, Director of Research, Civic

***"We need to set up procedures or methods to limit spending, or somehow tie spending to the revenues that are realistically available. . . . Another possibility would be to consolidate agencies."***

***— Richard S. Winder, Director, State & Local Taxes Household International***

*See Illinois Tax Policy on page 7*

*Illinois Tax Policy from page 6*

Federation; Don Haider, Director, Kellogg School of Management, Northwestern University; J. Thomas Johnson, National

*Patrick Quinn, Treasurer, State of Illinois*

Director - State and Local Taxes, Grant Thornton; Sen. Martin J. Butler, Appropriations Committee, Illinois General Assembly; Rep. Barbara Flynn Currie, Chairman, House Revenue Committee, Illinois General Assembly; Fred H. Montgomery, Senior Tax Attorney, Sara Lee Corporation; and Paul M. Green, Director, Institute for Public Policy, Governors State University.

Both Sen. Butler and Thomas Johnson remarked ruefully that the state seems to do its planning on a 24-hour basis. Johnson urged a more farsighted approach, not just on the revenue side, where complaints about inaccurate estimates have been heard in state capitals throughout the nation, but also on the spending side, where the pattern of rapidly accelerating expenditures, especially on Medicaid and corrections, is well established but often shunted aside as too unpleasant to face.

Butler said the state must consider business as an equal partner with labor and the state government. Until they do so and prove that the state has "a legislature that business can believe in and that has some understanding of what keeps a business thriving," Illinois will not achieve long-term economic growth.

Montgomery singled out the franchise tax as a major deterrent to capital formation and economic growth in the state, while Paul Green said, "My solution is simple: we need fewer people in state government; we need them to work harder; and we need to be able to hire and fire them." ■

***"I frequently hear that the income tax rates in Illinois are low, but we have to keep in mind that the base is relatively broad."***

***— Fred H. Montgomery, Senior Tax Attorney, Sara Lee Corporation***

FOUNDATION MESSAGE

## "Tax Fairness "and Tax Facts

***Dan Witt***
***Executive Director***

As Soviet political events unfold more dramatically each day, the tax policy scene in Washington is in the midst of a typically sleepy August. Congress led the charge of vacationers leaving town, but unlike recent August recesses when their departure broke off heated budget negotiations, 1991 has been a year of rhetorical sparring between Republicans and Democrats as they probe for weaknesses to exploit on the hustings in 1992.

"Tax fairness" is the label put on a variety of acrimonious charges the parties have been exchanging. Since the Tax Foundation has been monitoring government taxation as objectively as possible for more than fifty years, we are in a good position to referee such an argument.

The allegation is often repeated that tax legislation has dramatically changed the percentage of taxes paid by different income classes. After all, we have had so many major tax bills passed in the last decade, it does seem to make common sense that the balance of the tax burden would shift. Some say the middle class has borne the brunt of higher taxes, especially as Social Security rates have risen sharply, and the percentage of the median family's income subject to Social Security taxes has risen from 70 to 140 percent.

Just as often we hear that the poor got the worst of the eighties -- higher excise and sales taxes are usually the culprit here. And although the average person probably has less sympathy with the tax troubles of wealthier Americans, the eighties saw the demise of hundreds of tax loopholes and incentives, and the decade ended with a new higher income tax rate for approximately the top two percent of taxpayers.

So how do all these claims sort out? The simplest answer is that they're all right — *everyone* is paying higher taxes. Total taxes as a percentage of total income is 35.1 percent in 1991, the largest fraction of the economy to be commandeered by government in U.S. history. But as the cost of government grows, so too does the need to know who is picking up the biggest share of the bill.

One big clue is the annual release of federal individual income tax return data. For tax year 1989, just released, it shows conclusively that the distribution of the tax burden has not shifted dramatically over the course of the decade (see article on page 1). The portion paid by the top half has varied less than two percent, while the share paid by the top ten percent has grown slowly from a low of 48 percent in 1981 to a high of 56.9 percent in 1988, before ticking down slightly to 54.5 percent according to the new 1989 data.

Of course, federal income taxes are not the whole fairness picture, and the Foundation is currently undertaking an exhaustive study of the total federal and state tax burden by income class by state. We look forward to helping the public with our research to understand in the most complete way possible who is bearing the burden of American taxes.

## Next in Series of State Tax Policy Seminars To Be Held in Pittsburgh October 8

**8:30 a.m.** Registration/Coffee

**9:00-11:45** *Welcome:*
Dan Witt, Executive Director
Tax Foundation

*Moderator:*
William Flanagan, Money Editor
KDKA - TV

*Speakers:*
Catherine Baker Knoll, Treasurer
State of Pennsylvania

John Dankosky, Executive Director
Pennsylvania Business Roundtable

Michael H. Herschock,*
Budget Secretary
State of Pennsylvania

Rep. Joseph R. Pitts,* Republican
Chair, Appropriations Committee
Pennsylvania General Assembly

Stuart Hoffman,*
Chief Economist
Pittsburgh National Bank

Don Eberly
President, Commonwealth Foundation

Lewis B. Lee, Director - State Division
Pennsylvania Economy League, Inc.

Albert E. Germain,
Vice President Taxes & Tax Counsel
ALCOA

John D. Luffe, Director of U.S. Taxes
PPG Industries, Inc.
Chairman, Tax Committee,
Pennsylvania Chamber of Business & Industry

Robert P. Strause,
School of Urban and Public Affairs
Carnegie Mellon University

Charles L. Potter, Partner; CPA
Rose, Schmidt, Hasley & DiSalle

**12:00-1:30** Luncheon
Speaker to be announced

*Invited

# Floyd Williams Joins Tax Foundation As Chief Tax Counsel

Floyd L. Williams, III has joined the Tax Foundation's staff as chief tax counsel. He comes with a variety of Washington tax law experience, most recently as staff vice president and legislative counsel for the National Association of Home Builders. He supervised the writing of all proposed legislation, Congressional testimony and statements. He maintained contact with government agencies, Members of Congress, and congressional staffs, and supervised the preparation of articles, newsletters, and conference presentations, which kept members apprised of legislative developments.

Before joining the Home Builders, he spent two years with Coopers & Lybrand as a senior tax manager for their National Tax Consulting Group. There he dealt primarily with partnerships, tax-exempt bonds, and tax shelter issues.

Mr. Williams' stint at Coopers & Lybrand was preceded by eleven years of government service, four years at the Internal Revenue Service and seven years with the Joint Committee on Taxation.

Mr. Williams received his law degree from the University of Arkansas after attending the University of Virginia for his undergraduate degree. He received his LL.M. in taxation at the Georgetown University Law Center in 1977.

*Floyd L. Williams, III*

**Tax Features**

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